

# HOUSE BILL REPORT

## SHB 2192

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### As Amended by the Senate:

**Title:** An act relating to the Washington state teachers' retirement system.

**Brief Description:** Correcting the teachers' retirement system plan III.

**Sponsors:** By House Committee on Appropriations (originally sponsored by Representatives Carlson, Sehlin, H. Sommers, Cooke, Ogden, Dickerson, Dyer and Conway; by request of Joint Committee on Pension Policy).

### Brief History:

#### Committee Activity:

Appropriations: 1/19/96, 1/30/96 [DPS].

#### Floor Activity:

Passed House: 2/8/96, 84-10.

Senate Amended.

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### HOUSE COMMITTEE ON APPROPRIATIONS

**Majority Report:** The substitute bill be substituted therefor and the substitute bill do pass. Signed by 30 members: Representatives Huff, Chairman; Clements, Vice Chairman; Pelesky, Vice Chairman; H. Sommers, Ranking Minority Member; Valle, Assistant Ranking Minority Member; Basich; Beeksma; Brumsickle; Carlson; Chappell; Cooke; Crouse; Dellwo; Dyer; Foreman; Grant; Hickel; Jacobsen; Kessler; Lambert; Linville; McMorris; Poulsen; Reams; Rust; Sehlin; Sheahan; Silver; Talcott and Wolfe.

**Minority Report:** Do not pass. Signed by 1 member: Representative Hargrove.

**Staff:** Elissa Benson (786-7191).

**Background:** State law creates separate retirement systems for different groups of public employees. In many instances, employees of the same group who were initially hired at different dates participate in different plans of the same retirement system. The different plans of the same retirement system have differing retirement benefits and requirements.

Retirement systems can generally be classified as either a defined benefit system or a defined contribution system, based upon the nature of the retirement benefit. Under a

defined benefit system, a retiree receives a monthly benefit that is based upon the number of years of service in the system and a percentage of the average of his or her highest annual compensation. Under a defined contribution plan, an employee selects from a number of investment programs where contributions will be invested. The retirement benefits are based upon the amount of contributions and the earnings of the particular investments that are selected.

Three separate plans for the Teachers Retirement System (TRS) exist. Teachers who were initially hired prior to October 1, 1977 are members of TRS Plan I. Teachers who were initially hired on or after October 1, 1977 are members of TRS Plan II. Both TRS I and TRS II are defined benefit systems.

TRS III was enacted during the 1995 Legislative Session and is effective July 1, 1996. The purpose of TRS III is to give vested employees more flexibility in determining the form and timing of their retirement benefits and to allow employees to change careers without a dramatic loss of retirement benefits. TRS III has two components: 1) a defined benefit component paid by the employer, and 2) a defined contribution component paid by the employee. This two-component approach is different from the Plan II retirement system, in which the employer and employee contributions are both used for the purpose of providing the defined retirement benefit.

After reviewing issues regarding the implementation of TRS III, the Joint Committee on Pension Policy made a number of policy and administrative recommendations regarding TRS III, including the timing of the establishment of the Employee Retirement Benefits Board; the authority for substitute teachers to transfer to TRS III; the period for transfer from TRS II to TRS III; the selection of employee-defined contribution rates; the restoration of service credit upon return to service; the allocation rules for service credit purchases; the authority for educational aides to transfer to TRS III; the clarification of administrative and investment expense; and technical corrections.

#### Employee Retirement Benefits Board

The Employee Retirement Benefits Board was created by Plan III to make administrative decisions such as determining benefit distribution options and preselecting self-directed investment vehicles for members. The Employee Retirement Benefits Board will replace the Deferred Compensation Board and continue its duties along with new responsibilities associated with TRS III. Appointments to the board are to be made on TRS III's effective date, July 1, 1996.

#### Transfers of Substitute Teachers

Substitute teachers cannot transfer from Plan II to Plan III.

#### Transfer requests after the close of the transfer incentive payment period

TRS II employees may choose to transfer to Plan III between the effective date of the act, July 1, 1996, and January 1, 1998. Employees who transfer during that period will receive a 20 percent increase to their employee contributions accumulated through January 1, 1996. The act did not address how requests to transfer to Plan III will be handled after the transfer incentive payment period closes.

#### Selection of employee-defined contribution rates

Plan III requires members to make an irrevocable choice of defined contribution rate structure. The Internal Revenue Service allows members to change defined contribution rates when they change employers within the same retirement plan.

#### Restoration of service credit upon return to service

Members have a right to a benefit at retirement, if they meet certain age and service requirements. Members who do not meet the benefit eligibility requirements, leave employment, then return to work, must work 12 consecutive months to regain credit for past service. Under the 12-month requirement, members with intermittent employment could work 10 or more years without vesting.

#### Allocation rules for service credit purchases

To purchase certain kinds of service credit, such as unpaid leave of absence, or to restore service credit after statutory time limits, members pay more than just employee contributions. Plan III does not determine how these payments should be allocated between the defined benefit trust fund and the defined contribution plan member account.

#### Transfer to TRS III of education staff associates who are currently PERS II

Education staff associates who are members of PERS II are not permitted to transfer to TRS III.

#### Administrative and investment expenses

For other retirement system plans administered by the Department of Retirement Systems (DRS), administrative expenses are paid from the DRS expense fund, which is funded by employer fees. Employees do not pay for administrative fees. Payment of administrative and investment expenses incurred by the DRS and the State Investment Board (SIB) in the administration of members' defined benefit accounts and defined contribution accounts is unclear.

### Structure of Retirement Funds

Under current law, there is a separate account within the state treasury which consists of all TRS III employee contributions and associated investment earnings.

### Access to health care benefits upon retirement or separation

Under current law, K-12 retirees can purchase benefits through the Health Care Authority if they receive a retirement benefit immediately upon separation. This means that if an employee terminates employment, but officially retires at a later date, the employee loses his or her opportunity to purchase benefits at a subsidized rate through the Health Care Authority.

### **Summary of Bill:**

#### Employee Retirement Benefits Board

Appointments to the Employee Retirement Benefits Board can occur upon the effective date of this act.

#### Transfers of Substitute Teachers

Substitute teachers may transfer from Plan II to Plan III, effective any month for which they purchase service credit. Substitute teachers who establish service credit for January 1998, establish any service credit from July 1996 through December 1997, and transfer on or before March 1, 1999, will have their member contributions increased by 20 percent.

#### Transfer requests after the close of the transfer incentive payment period

Members who request to transfer to Plan III on or after January 1, 1998, will be able to do so during a month-long open window period each January. They will not receive an incentive payment.

#### Selection of employee-defined contribution rates

Members who change employers may change defined contribution rates consistent with Internal Revenue Service standards. Change of employer means change of agency or school district.

#### Restoration of service credit upon return to service

Members who return to work have their previous service credit immediately restored without having to earn additional service credit. Members who leave employment

have the right to a normal retirement benefit if they are age 65 and they have 1) 10 years of service; or 2) five years of service, including one year of service after age 54.

Allocation rules for service credit purchases

Employee payments for service credit purchase or restoration transferred from TRS II service credit will be allocated as follows. Employer contributions paid by members are deposited in the Plan III defined benefit trust fund. Employee payments for restored service credit will be split equally between the defined contribution account and the defined benefit account.

Transfer to TRS III of education staff associates who are currently PERS II

Education staff associates who are members of PERS II have until January 1, 1998, to request transfer to TRS III.

Administrative and investment expenses

With the exception of legal and medical expenses provided for under RCW 41.50.255 and expenses associated with the defined contribution accounts that are self-directed, administrative expenses for both the defined benefit and defined contribution parts of TRS III will be paid from the DRS expense fund which is funded by employer fees, as is the practice for other retirement systems administered by DRS.

Members that elect to self-direct investments must pay the investment expenses associated with self-directed investments.

Access to health care benefits upon retirement or separation

TRS III members who separate from employment after age 55 with at least 10 years of service have two opportunities to purchase benefits through the Health Care Authority at a subsidized rate. The first opportunity is immediately upon separation; the second opportunity is immediately upon receiving a retirement benefit.

**EFFECT OF SENATE AMENDMENT(S):** The Senate amendment eliminates a separated TRS III member's second opportunity to purchase health care benefits through the Health Care Authority at a subsidized rate when a separated member accesses his or her retirement benefit, typically at age 65. A TRS III member who separates from employment at age 55 with at least 10 years of service will still have the opportunity to purchase health care benefits through the Health Care Authority at a subsidized rate immediately upon separation.

**Appropriation:** None.

**Fiscal Note:** Available.

**Effective Date:** The bill contains an emergency clause and takes effect immediately.

**Testimony For:** Teachers support this bill but would like to see provisions made for one-on-one financial counseling for those TRS II members who are trying to decide on whether to transfer to TRS III.

**Testimony Against:** None.

**Testified:** Bob Maier, Washington Education Association.